



A PHI Company

March 29, 2010

VIA HAND DELIVERY

Ms. Alisa C. Bentley, Secretary
Delaware Public Service Commission
861 Silver Lake Boulevard
Cannon Building, Suite 100
Dover, DE 19904

**RE: In the Matter of the Application of Delmarva Power & Light
Company for Approval of a Change in Electric Distribution Base
Rates and Miscellaneous Tariff Changes
PSC Docket Nos. 09-414/ 09-276T**

Dear Ms. Bentley:

Enclosed for filing please find the original and 10 copies of the following testimony:

1. Public Version of the Supplemental Rebuttal Testimony of Anthony J. Kamerick,
2. **Confidential- Non-Public** Version of the Supplemental Testimony of Anthony J. Kamerick
(filed pursuant to Rule 11 of the Commission's Rules of Practice and Procedure) and
3. Rebuttal Testimony of Steven M. Fetter.

This testimony consists of Delmarva's response to the issue of "Ring Fencing," introduced by Staff's Liberty Consulting witnesses in the above referenced Docket.

Pursuant to Rule 11, I hereby attest that the information redacted from the Public Version of the testimony of Mr. Kamerick, and which is included in the Confidential Version of the same testimony, is not subject to inspection by either the public or by other parties. Counsel for parties who have executed the appropriate confidentiality agreement will be provided with the Confidential Version.

As always, should you have any questions please contact me at (302) 429-3786

Respectfully Submitted,

Todd L. Goodman

cc: Service List – Overnight Mail and Email (Public Version Only)

STEVEN M. FETTER

1 **DELMARVA POWER & LIGHT COMPANY**
2 **REBUTTAL TESTIMONY OF STEVEN M. FETTER**
3 **BEFORE THE DELAWARE PUBLIC SERVICE COMMISSION**
4 **CONCERNING AN INCREASE IN ELECTRIC BASE RATES**
5 **DOCKET NOS. 09-414/09-276T**

6 **I. Introduction**

7 1. Q: Please state your name and business address.

8 A: My name is Steven M. Fetter, and my business address is 1489 West
9 Warm Springs Road, Suite 110, Henderson, NV 89014.

10 2. Q: By whom are you employed and in what capacity?

11 A: I am President of Regulation UnFettered, an energy advisory firm I started
12 in April 2002. Prior to that, I was employed by Fitch, Inc. (Fitch), a credit rating
13 agency based in New York and London. Prior to that, I served as Chairman of the
14 Michigan Public Service Commission (Michigan PSC).

15 3. Q: What is the purpose of your rebuttal testimony?

16 A: Delmarva Power & Light Company (Delmarva or Company), with parent
17 holding company Pepco Holdings Inc. (PHI), has asked me to review and
18 comment on the direct testimony of Messrs. John Antonuk and Randall Vickroy
19 of The Liberty Consulting Group (collectively, Liberty), filed in this proceeding
20 on behalf of the Delaware Public Service Commission (Commission) Staff. In
21 this rebuttal testimony, I respond to the recommendation made by Liberty that the
22 Commission should impose certain "ring-fencing" conditions on Delmarva. I
23 disagree with many of the statements made by Liberty, which I will discuss
24 specifically within this testimony.

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1 bond issuer as well as additional quantitative and qualitative information gathered
2 from third-party sources.

3 7. Q. **What was your role during your employment with Fitch?**

4 A. I was Group Head and Managing Director of the Global Power Group
5 within Fitch. In that role, I served as group manager of the combined 18-person
6 New York and Chicago utility team. I was originally hired to interpret the impact
7 of regulatory and legislative developments on utility credit ratings, a
8 responsibility I continued to have throughout my tenure at the rating agency. I
9 was employed by Fitch from October 1993 until April 2002. In April 2002, I left
10 Fitch to start Regulation UnFettered. Shortly after I resigned, Fitch retained me
11 as a consultant for a period of approximately six months.

12 8. Q. **Was there any aspect of your experience at the Michigan PSC that**
13 **particularly relates to your testimony in this proceeding?**

14 A. Yes. During my six years at the Michigan PSC, my colleagues and I
15 sought to effectuate policies that were fair to all stakeholders and which would
16 encourage regulated utilities to provide customers with reliable utility service in a
17 cost-effective manner. We also sought to ensure that the financial health of the
18 state's utilities would remain sufficient for them to be able to provide reliable
19 service to all consumers, and also that investors would maintain their interest in
20 providing necessary funding on a timely basis upon reasonable terms. On this
21 latter point, while seeking to be sensitive to the concerns of consumers within
22 Michigan, we always endeavored to respect the interests of the institutional
23 investors that provided needed capital to the state's utilities.

1 Achieving these goals requires regulators to successfully strike a difficult
2 balancing of interests. Investors provide financing to a utility so that company
3 management can construct and maintain infrastructure adequate to ensure that
4 customers will receive reliable service. In return, regulators must take timely
5 action to provide an appropriate capital markets-based return to investors along
6 with providing reimbursement of company expenditures that are prudently made.
7 A failure to carry out these regulatory responsibilities in a consistent and
8 predictable manner will ultimately be detrimental to both investors and customers,
9 as investors will choose to take their funds elsewhere. Similarly, regulators need
10 to be mindful in exercising regulatory authority over public utilities that
11 inconsistent or unwarranted rules, regulatory policies or conditions could result in
12 risks to investors that could chill their interest in investing in a particular
13 jurisdiction.

14 I believe that the circumstances surrounding my regulatory and utility
15 rating experience that I have described above are relevant to the issues before the
16 Commission in this proceeding, and I will further elaborate upon these points
17 within the remainder of my testimony.

18 9. Q. Please describe your other prior professional experience related to the utility
19 industry.

20 A. During my time on the Michigan PSC, I served as Chairman of the Board
21 of Directors of the National Regulatory Research Institute (NRRI) at Ohio State
22 University, the regulatory research arm of the 50 state and District of Columbia
23 public utility commissions. In 2003, I was appointed by the President of the

1 National Association of Regulatory Utility Commissioners (NARUC) to serve as
2 a public member of the NRRI Board – the 20-member governing board included
3 ten state public utility commissioners. I was reappointed to the NRRI Board for a
4 three-year term in June 2005, and again in 2008 to the inaugural Board of NRRI
5 upon its relocation to Washington, DC.¹ I also have served on the Keystone
6 Center Energy Board (a nonprofit public policy board that brings together diverse
7 stakeholders related to the regulated utility industry as well as appointed and
8 elected federal and state policymakers to discuss challenges facing the sector),
9 after having participated in the Keystone Center Dialogues on Financial Markets
10 and Energy Trading and on Regional Transmission Organizations. In February
11 2002, I was appointed to the Board of Directors of CH Energy Group, Inc.
12 (CHG), the parent company of Central Hudson Gas & Electric in Poughkeepsie,
13 New York. I currently serve as Lead Independent Director of the CHG Board and
14 also Chairman of the CHG Governance and Nominating Committee, having
15 previously served as Chairman of the Audit Committee and the Compensation
16 and Succession Committee.

17 **10. Q. Have you previously sponsored testimony before regulatory and legislative**
18 **bodies?**

19 A. Since 1990, I have on numerous occasions testified before the U.S. Senate,
20 the U.S. House of Representatives, the Federal Energy Regulatory Commission
21 (FERC), federal district and bankruptcy courts, and various state legislative,
22 judicial, and regulatory bodies on the subjects of credit risk within the utility

¹ I resigned from the NRRI Board in 2009 when NRRI entered into a contract with the Hawaii Public Utilities Commission to serve as staff support for a rate case within which I testified as a witness on behalf

1 sector, electric and natural gas utility restructuring, utility securitization bonds,
2 fuel and purchased power and other energy adjustment mechanisms, and nuclear
3 energy. My full educational and professional background is attached in Schedule
4 SMF RF-1.

5 **11. Q. In the context of your broad experience within the regulated utility sector,**
6 **what prior involvement have you had with the concepts of ring fencing or**
7 **other corporate separation issues related to affiliated regulated and**
8 **unregulated utility operations?**

9 A. I have been involved with such issues throughout my utility career. As a
10 state regulator, I dealt with Consumers Power's spin-off of its abandoned Midland
11 nuclear plant into the largest unregulated cogenerator in the U.S. (with 50%
12 ownership remaining at the utility's unregulated parent). As a bond rater, I served
13 on the Fitch utility securitization team, whose key focus was working with utilities
14 to structure securitization transactions that enhanced utilities' financial strength,
15 ameliorated customer rate impact and, at the same time, provided investors with
16 protection from any negative ramifications that could result if a utility was forced to
17 file for bankruptcy protection. Later, as a consultant, my views on ring fencing were
18 published in an opinion piece in Public Utilities Fortnightly.² That led to the
19 California Public Utilities Commission's inviting me to testify within their 2006
20 rulemaking docket related to energy utility holding company affiliate relations.³

of Hawaiian Electric Company.

² "Perspective: Don't Fence Me Out," Public Utilities Fortnightly (Oct. 2004).

³ California Public Utilities Commission, Docket No. R.05-10-030: Rulemaking Concerning Relationship Between California Energy Utilities And Their Holding Companies And Non-Regulated Affiliates (issued Sept. 21, 2006).

1 **III. REBUTTAL OF LIBERTY'S RING-FENCING PROPOSALS**

2 12. Q. **Have you reviewed the Direct Testimony of Liberty that has been filed in this**
3 **proceeding?**

4 A. Yes, I have.

5 13. Q. **In its direct testimony, Liberty discusses the origins of ring fencing, the goals**
6 **of ring fencing, and, as seen by Liberty, ring fencing's effectiveness. Liberty**
7 **seems to imply that perhaps all holding companies comprised in part with**
8 **regulated utilities, including PHI, should be subject to ring fencing. Would**
9 **you agree with this strategy for the industry?**

10 A. No, I would not, and I base my view on what I have seen as a state utility
11 regulator, utility bond rater, and now a consultant for regulated utilities,
12 commissions, and consumer advocates. All current utility holding companies
13 have been established pursuant to and consistent with relevant federal and state
14 laws. If the entire industry structure were to be unwound to provide corporate
15 separation for all regulated utilities, the costs would be enormous and a
16 substantial amount of utility industry managerial expertise would be shut off from
17 assisting with the effective operation of regulated utilities. The costs that would
18 accompany such ring-fencing mandates would have to settle somewhere. I
19 disagree strongly with Liberty's assertions that such additional costs should not be
20 placed into regulated rates. As alluded to above, PHI and Delmarva are operating
21 under a holding company structure that is permitted under existing federal and
22 state law. Any actions by state regulators to require Delmarva to modify its

1 current lawful framework will result in costs related to regulatory compliance and
2 therefore should be recoverable within regulated rates.

3 However, regardless of how those costs are treated, their mere existence
4 coupled with the walling off of experienced utility management personnel from
5 regulated operations would introduce inefficiencies into the regulated utility
6 sector. Accordingly, I believe that ring fencing should only be considered where
7 traditional regulatory policies are ineffective, as in a case where the management
8 of a holding company comprised of both regulated and unregulated entities
9 maintains a belligerent attitude toward regulators and their policies, or where
10 affiliates of the holding company are involved in especially risky unregulated
11 behavior and activities. As explained in extensive detail in Company Witness
12 Kamerick's supplemental rebuttal testimony, PHI, and Delmarva, in no way fall
13 into this category.

14 **14. Q. Major focuses of Liberty's direct testimony are the situations that confronted**
15 **Enron/Portland General Electric Company and Constellation Energy, which**
16 **Liberty argues supports strong ring-fencing conditions for PHI and**
17 **Delmarva. Do you see relevance to those negative experiences and the**
18 **circumstances that PHI and Delmarva faced during the recent financial**
19 **crisis?**

20 **A.** No, I do not. The majority of major ring-fencing efforts among U.S.
21 regulators concerned particular unquantifiable risks that arose in the context of
22 acquisitions, mergers and spin-offs, and then usually only when the proposed
23 transaction involved complex fact patterns. For instance, the ring-fencing

1 situations that I have worked on have involved major transactions with unusual
2 circumstances: Iberdrola, one of the world's largest utilities, undertaking a cross-
3 border acquisition of a U.S. utility holding company and its two regulated utilities
4 (Energy East, New York State Electric & Gas, and Rochester Gas & Electric), and
5 the largest private equity takeover of a major U.S. regulated utility (TXU).
6 Indeed, the two examples Liberty points to exhibited fact patterns indicating
7 substantial uncertainty going forward: Enron, one of the most aggressive and
8 risky global energy players acquiring Portland General Electric, a small regulated
9 utility company, and Constellation Energy (Constellation), an extremely
10 aggressive national energy marketer which suffered due to the limited spread of
11 electricity competition and a financial crisis that threatened its viability going
12 forward, leading it to be "saved" initially by a large investment by MidAmerican
13 Energy, with announcement of a potential merger of the two entities. Thereafter,
14 in mid-December 2008, Constellation backed out of the MidAmerican merger, at
15 least in part due to investor sentiment that the deal had been done at a fire-sale price
16 due to the credit crisis, and instead agreed to sell half of its nuclear power business
17 to Electricite de France SA for \$4.5 billion.⁴

18 Inexplicably, Liberty, in its direct testimony, only gets half of this story right
19 when it states:

20 Ultimately, MidAmerican agreed to make an immediate preferred
21 stock investment of \$1 billion, and to buy Constellation for \$26.50 per
22 share in an all-cash merger. Thus, the liquidity crisis caused by
23 Constellation's trading operations forced the sale of the holding
24 company at a bargain price. (Liberty Direct Testimony at 10)

⁴ See "EDF Beats Out Buffett in Energy Deal," Wall Street Journal, December 17, 2008.

1 As discussed above, the sale of the holding company was terminated and never
2 occurred. More relevant is that Liberty is accurate when it acknowledges that
3 “The dollar magnitude of the liquidity shortfalls at PHI was significantly less than
4 that of Constellation” (Liberty Testimony at 11), and that PHI’s approach to
5 address its liquidity concerns was “sound” (Liberty Testimony at 15).

6 **15. Q. I want to return to liquidity in a moment. But first do you believe that**
7 **Delmarva’s regulated utility customers have to be shielded from PHI’s**
8 **unregulated activities?**

9 A. No, I do not. Delmarva is a subsidiary of PHI. PHI’s subsidiaries are
10 substantially in traditionally regulated utility businesses. This point is made in
11 PHI’s 2009 Form 10-K filed with the U.S. Securities and Exchange Commission
12 (SEC) which states on page 2 that 73% of PHI’s consolidated operating income
13 comes from the holding company’s regulated power delivery business. In
14 addition, in presentations to the financial community, PHI management has
15 emphasized that its earnings base is “derived primarily from growing regulated
16 utility business” and that it is committed to investment grade credit quality,
17 improved liquidity, and a focus on lowering business risk.⁵ The rating agencies
18 also confirm the highly regulated nature of PHI’s business. For example, the S&P
19 report on Delmarva dated August 6, 2009 states that “PHI’s business risk profile
20 is considered strong after incorporating the excellent business profiles of the rated
21 utilities, including [Delmarva], and the company’s more risky unregulated
22 operations.” S&P does acknowledge that it considers the unregulated businesses

⁵ See, for example, PHI Presentation: “Managing Today’s Challenges: Positioning for Tomorrow’s Growth,” 44th Edison Electric Institute Financial Conference, Hollywood, Florida, November 1-4, 2009.

1 “significantly more risky than the utilities due to their exposure to volatile
2 commodity prices and very competitive energy markets,” but does gain some
3 comfort from PHI’s “strategy to hedge a majority of its capacity over a two-to
4 three-year period.”⁶ I see little similarity between the Enron/Portland General
5 Electric and Constellation situations and the circumstances under which PHI and
6 Delmarva operate.

7 **16. Q. Do you believe that Liberty’s discussion of ring-fencing issues in this**
8 **proceeding comes at a particularly inopportune time?**

9 A. Yes, I do. The U.S. stock market experienced its third worst year in more
10 than a century in 2008, with the S&P 500 and the Dow Jones Industrial Average
11 down 38.5% and 33.8%, respectively. No fewer than fifteen U.S. banks failed in
12 2008, including the well-publicized bankruptcy of Lehman Brothers on
13 September 15, 2008, the largest bankruptcy in U.S. history. The changes on Wall
14 Street mean that there is less capital available for companies seeking debt and
15 equity financing – and, unlike the broader corporate industrial sector which can
16 delay capital investment during times of duress, regulated utilities carry a public
17 responsibility to expend capital when needed to ensure safe and reliable service to
18 customers. Indeed, even when short-term credit was available during the
19 financial crisis, it was often at significantly higher costs and upon less favorable
20 terms and conditions. As Moody’s reported in a January 16, 2009 report entitled,
21 “Near-term Bank Credit Facility Renewals To Be More Challenging For U.S.
22 Investor-Owned Electric and Gas Utilities”:

⁶ S&P Research: “Delmarva Power & Light Co.,” August 6, 2009.

1 Dramatic changes in the financial markets during 2008 have
2 materially changed the banking environment for utilities going
3 forward, which will make upcoming credit facility renewals
4 significantly more challenging. . . . Those banks that do remain
5 will be constrained in both their ability and inclination to provide
6 traditional credit, especially at the relatively low pricing levels and
7 on the liberal terms and conditions that prevailed prior to mid-
8 2008.
9

10 **17. Q. How do the stresses flowing from the financial crisis fit with Liberty's**
11 **proposals?**

12 A. Liberty, after a discussion of various credit rating agency ring-fencing
13 notching policies, settles upon a position that calls for Delmarva's return on
14 equity and customer rates to be set based upon an S&P rating of "BBB+", rather
15 than its current corporate rating of "BBB". Unfortunately, the appropriate
16 equation is not that simple. While ring fencing might provide a degree of comfort
17 for debt investors considering providing funds to Delmarva, it would have the
18 opposite effect on both equity and debt investors in PHI, since costs at both PHI
19 and Delmarva would go up and access to earnings from the regulated utility could
20 potentially be restricted in the future. Such circumstances would result in a higher
21 cost of equity for both PHI and Delmarva, with the higher costs for Delmarva
22 ultimately translating into higher rates for customers. Thus, any savings from
23 Liberty's suggested uptick in Delmarva's ratings, a speculative assumption,
24 would probably be outweighed by a higher cost of equity for the Company that
25 would be virtually certain to occur within a ring-fenced corporate structure. In
26 addition, the existing framework which currently provides attractive funding
27 vehicles for the benefit of Delmarva, as described in the supplemental rebuttal

1 testimony of Company Witness Kamerick, would be undermined if ring fencing
2 were to limit their availability.

3 In view of the turmoil that has characterized the credit markets during the
4 past year-and-a-half and which still creates volatility within the equity markets,
5 actions by a regulator creating the perception that it is asserting control over a
6 utility's internal operations, including most notably both regulated and
7 unregulated Board of Director processes, to possibly eke out a slight credit rating
8 bump, does not appear to be a reasonable strategy under current economic
9 conditions. This is especially so when the actions are not taken in the context of
10 approving a transforming transaction, but rather emerge within a proceeding
11 focused on a normal request for rate relief. Likewise, actions that would establish
12 a perception that the regulator is creating barriers to the realization of efficiencies
13 and economies of scale from a utility's participation in a normal holding company
14 structure could cause additional concern and uncertainty in the investment
15 community. Notwithstanding the difficult conditions in the financial marketplace,
16 utilities and regulators are well-served by acting in concert to ensure that investors
17 view regulated utility companies as sound investments. It would be counter-
18 productive for the Commission to take actions that would have the opposite
19 effect.

20 **18. Q. Does Liberty indicate that its ring-fencing proposals would result in an**
21 **improved credit rating for Delmarva?**

22 **A.** Yes. While at first Liberty talks in terms of potential three-notch rating
23 gains, as I noted above, in the final analysis Liberty focuses in on movement of

1 S&P's Delmarva rating one-notch from "BBB" to "BBB+", basically eliminating
2 the effects of S&P's consolidated rating methodology. Unfortunately, what is lost
3 in this analysis is that institutional investors are fully aware of the consolidated
4 nature of S&P's ratings, so that they already view Delmarva's consolidated
5 "BBB" rating as somewhat stronger, and PHI's consolidated "BBB" rating as
6 somewhat weaker. This can be seen in S&P treating PHI and Delmarva
7 differently from each other with regard to unsecured debt, maintaining a senior
8 unsecured rating of "BBB" for Delmarva and "BBB-" for PHI.

9 That said, even erring on the side of Liberty's analysis and crediting
10 Delmarva with a "BBB+" rating does not support Liberty's argument. As I
11 discuss above, substantially limiting interaction between parent PHI and its
12 regulated Delaware subsidiary in order to possibly improve Delmarva's credit
13 ratings by a notch – but still within the "BBB" category – seems to me to be the
14 wrong action at the wrong time. Investor uncertainty would grow and economies
15 of scale would be lost, as would benefits that can flow from shared managerial
16 expertise. Rather than erecting barriers between Delmarva, PHI and the other PHI
17 subsidiaries, I believe both consumers and investors are better served by a smooth
18 functioning entity within which legitimate cost-sharing is utilized, along with
19 close interaction among all members of management. Such a framework does not
20 require legal ring fencing. Because PHI's businesses are currently regulated to a
21 substantial degree, they are subject to constant scrutiny by regulators – especially
22 with regard to cross subsidization issues – and the Commission holds clear
23 authority to protect consumers and prevent abuses.

1 **19. Q. Do Moody's and Fitch assign credit ratings in a similar manner to S&P?**

2 A. As far as S&P's consolidated methodology is concerned, the answer is no.
3 Both Moody's and Fitch assess Delmarva on a standalone basis, and then factor in
4 parent influence on the rating to a degree. For Moody's and Fitch, there is
5 typically a one notch differential between a regulated utility and its unregulated
6 parent to reflect the differing business and financial risk at each of the corporate
7 entities: here Moody's has Delmarva at "Baa2" and PHI at "Baa3"; Fitch rates
8 Delmarva at "BBB+" and PHI at "BBB".⁷ It is important to note that none of the
9 three major rating agencies have discussed a potential need for ring fencing within
10 the PHI/Delmarva corporate structure, nor have they posited any potential
11 benefits that could result from such aggressive regulatory action.

12 In view of the fact that PHI's business risk is relatively bounded now, I
13 would expect that significant ring fencing would not result in a major change in
14 Delmarva's ratings, especially since the variance in the parent's and subsidiary's
15 circumstances is already reflected in the existing one notch difference in ratings.
16 Moreover, as I discuss above with regard to S&P, even if another ratings notch
17 could be achieved through extensive ring fencing, I believe the restrictions
18 necessary to secure such gain would not represent a beneficial tradeoff.

19 **20. Q. Turning back to liquidity, can you comment upon this important issue as it**
20 **affects PHI and its regulated subsidiaries?**

21 A. Yes. Liberty focuses on a PHI level liquidity crisis that occurred in 2008.
22 As I discuss above, the financial crisis that all businesses worldwide endured in
23 that timeframe was a once in a century occurrence, basically something that a

1 rational business cannot, indeed should not, structure its business to repel on an
2 ongoing basis. To do so would be to hamstring a company's productivity and
3 efficiency while waiting for the proverbial lightning to strike. Rather all
4 companies had to react to the extraordinary event in an effort to ensure survival
5 and self-preservation. That is what PHI did. Company Witness Kamerick
6 provides substantial detail about the tough choices PHI and Delmarva had to
7 make to preserve their liquidity and financial stability during the crisis, and now
8 going forward. S&P in a report issued August 6, 2009 confirms the wisdom of
9 the path PHI took on the crucial liquidity issue:

10 [Delmarva's and PHI's short-term rating] reflects [S&P's]
11 expectation that PHI will retain an adequate level of availability
12 under its credit facilities for liquidity requirements and any cash
13 collateral calls. ... The company has maintained sufficient liquidity
14 to address potential collateral calls under a stressed scenario
15 comprised of a negative credit event and an adverse movement in
16 commodity prices.⁸
17

18 I could envision a possible argument that actions taken by a regulated utility
19 during the financial crisis to preserve liquidity and financial stability could be
20 deemed prudent even though those actions failed. However, I would be hard-
21 pressed to make the case, as Liberty attempts here, that the successful steps
22 Delmarva took to confront its once-in-a-lifetime financial challenge could be
23 deemed inappropriate.

24 **21. Q. Liberty provides a list of recommended ring-fencing conditions. Would you**
25 **offer your views with regard to them?**

26 **A. Yes. With regard to the specific provisions proposed by Liberty:**

⁷ See Moody's Research: "Rating Methodology – Regulated Electric and Gas Utilities," August 2009.

⁸ S&P Research: "Delmarva Power & Light Co.," August 6, 2009.

1 1) “[Delmarva] shall not make any distributions that would cause its equity
2 capital to fall below 40 percent of permanent capital.”

3 ■ It is my understanding that PHI and Delmarva management organize their
4 distributions in order to prevent such an eventuality. For example,
5 Delmarva’s equity capital has varied between 44.5% and 50.5% during the
6 past five years, with the highest equity ratio – 50.5% – coming as of
7 December 31, 2009. In any event, the Company believes that the
8 Commission holds sufficient remedies to deal with such action by
9 Delmarva through its traditional statutory ratemaking authority.

10 2) “[Delmarva] may not participate in any money pool that involves non-utility
11 businesses, operations, or participation.” and

12 3) “PHI must create separate credit facilities for its utility subsidiaries, PHI and
13 its unregulated subsidiaries through solicitation processes that are completely
14 independent and wholly unconnected.”

15 ■ As explained in Company Witness Kamerick’s supplemental rebuttal
16 testimony, Delmarva’s participation in a money pool and involvement
17 with credit facilities provide benefits to the Company in a manner that
18 does not open Delmarva up to harm because of its involvement. To enter
19 into such financing vehicles on its own would be significantly more costly
20 for Delmarva and, through the ratemaking process, its customers.

21 4) “[Delmarva] and PHI must establish a bankruptcy-remote special purpose
22 entity or class of preferred stock that will protect [Delmarva] in the event of a
23 holding company bankruptcy.”

1 ■ I view this proposed provision as an extreme overreaction to PHI's and
2 Delmarva's circumstances. As S&P has recently noted, "In the case of
3 regulated electric, gas, and water utilities,... when the utility subsidiary
4 itself is not the cause of the parent's financial difficulties, it is rare for the
5 subsidiary to become directly entangled in a parent's bankruptcy
6 proceedings." Accordingly, S&P views the "likelihood of the subsidiary
7 being drawn into a parent's bankruptcy through substantive consolidation
8 [as] a relatively minor consideration ... in determining the relationship
9 between the ratings of a utility and its parent."⁹ Moreover, PHI's structure
10 bears no relation to the former Enron/Portland General Electric
11 framework. Indeed, a review of energy holding companies that have made
12 use of a special preferred stock or "golden share" arrangement during the
13 recent past shows a group of companies that possess international
14 relationships not relevant to PHI's situation, or holding companies with
15 markedly higher ratios of unregulated to regulated net income than does
16 PHI and its regulated subsidiaries: National Grid/Keyspan & Niagara
17 Mohawk; Iberdrola/Energy East & New York State Electric and Gas and
18 Rochester Gas and Electric; and Constellation Energy and Baltimore Gas
19 & Electric (as part of the Electricite de France nuclear asset investment).
20 In contrast to the regulatory proceedings within which ring-fencing
21 conditions were established for those holding companies, this proceeding
22 does not involve an acquisition, merger, or spin-off transaction. It is a

⁹ S&P Research: "Methodology: Differentiating the Issuer Credit Ratings of a Regulated Utility Subsidiary and Its Parent," March 11, 2010.

1 traditional utility rate case, the focus of which is on Delmarva's revenue
2 requirement, cost of service, and rate design. It would be very unusual for
3 a regulatory commission to impose such far-reaching ring-fencing
4 conditions on a utility as part of a normal rate case. This would be
5 especially so for a holding company like PHI which is not involved in a
6 corporate structure realignment through merger or other action, has no
7 international involvement, and currently produces approximately 73% of
8 its operating income from its regulated utility subsidiaries.

9 5) "Separate cash management systems must be maintained; those that involve
10 [Delmarva] must be separate and distinct from those of the holding company
11 and any non-utility affiliate." and

12 6) "[Delmarva] may not enter into any inter-company loans, guarantees or credit
13 support agreements with the holding company or any affiliate, nor may any
14 expectation of any form of utility support for non-utilities be created." and

15 7) "[Delmarva] must maintain separate accounting books and records using
16 systems separated from those of the holding company and all affiliates."

17 ■ It is my understanding that PHI and Delmarva practice financial
18 management activities that mirror each of these recommendations, as
19 explained in the supplemental rebuttal testimony of Company Witness
20 Kamerick.

21 8) "[Delmarva] and PHI must provide Commission access to all books, records,
22 documents, data, board minutes, presentations and forecasts of [Delmarva],
23 PHI and all PHI subsidiaries and affiliates."

1 ■ I believe regulatory access to information necessary to ensure appropriate
2 cost allocation to the regulated entity is appropriate and is currently
3 available to the Commission. At the same time, I do not believe that such
4 access should be treated as a license to prospect through the books and
5 records underlying the proprietary unregulated activities of the holding
6 company or other unregulated affiliates, as would certainly be the case
7 with the overreaching into PHI and unregulated subsidiary and affiliate
8 Board of Director activities and documents that Liberty proposes.
9 Moreover, even if the Commission and its staff intended that all of this
10 proprietary information would be treated confidentially, such protection is
11 often easier to promise than to deliver upon. Take, for example, reports
12 out of the SEC last year that some of their own regulatory attorneys were
13 meeting for weekly lunches to exchange stock-trading tips on companies
14 at various levels of agency scrutiny, upon which they sometimes acted.¹⁰
15 Such behavior where least expected makes me view this bad idea as even
16 worse than I could have envisioned prior to learning of such inappropriate
17 behavior at the federal agency charged with capital markets oversight.

18 9) "No [Delmarva] assets, financial support, or cash flow may be pledged or
19 used as collateral for the benefit of any entity except [Delmarva], and holding
20 company and affiliate financing agreements and arrangements must disclaim
21 any informal representation, commitment, or expectation of such support."

¹⁰ Wall Street Journal, "Insider Trading Probe at SEC," May 16, 2009.

1 ■ It is my understanding that these activities are prohibited by Delmarva's
2 Mortgage (see Company Witness Kamerick's supplemental rebuttal
3 testimony).

4 10) "[Delmarva] asset sales of greater than \$20 million must be approved in
5 advance by the Commission."

6 ■ As stated in Company Witness Kamerick's testimony, legislation is
7 currently in place in Delaware that governs Commission approval of
8 utility assets sales.

9 11) "[Delmarva] and PHI must establish an annual reporting process regarding the
10 status of each of the ring fencing requirements."

11 ■ As discussed by Company Witness Kamerick in his supplemental rebuttal
12 testimony, the Company would agree to annual reporting on the
13 considerable existing safeguards in place to maintain separation between
14 Delmarva and its affiliated companies.

15 IV. CONCLUSION

16 22. Q. Do you have concluding thoughts?

17 A. Yes. I see no reason for the Commission to institute an expansive ring-
18 fencing regime for a holding company that bears none of the indicia of risk that
19 characterized the companies that have become subject to ring-fencing restrictions
20 during the recent past. This is especially true in light of the uncertainty that
21 continues to exist within the capital markets. Every U.S. utility is now
22 endeavoring to maintain ready capital market access at reasonable cost, both on
23 the debt and equity sides. Springing ring-fencing policies out of a traditional rate

1 case would not make PHI's financing tasks any easier, especially on the equity
2 side – rather it would introduce an element of uncertainty within the minds of
3 investors as to what new regulatory policies might appear out of future
4 Commission proceedings.

5 **23. Q. Does this conclude your rebuttal testimony?**

6 A. Yes, it does.

7

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Education University of Michigan Law School, J.D. 1979
Bar Memberships: U.S. Supreme Court, New York, Michigan
University of Michigan, A.B. (Communications) 1974

April 2002 – Present

President – REGULATION UnFETTERED – Henderson, NV

Founder of advisory firm providing regulatory, legislative, financial, legal and strategic planning advisory services for the energy, water and telecommunications sectors, including public utility commissions and consumer advocates; federal and state testimony; credit rating advisory services; negotiation, arbitration and mediation services; skills training in ethics, negotiation, and management efficiency.

- Service on Boards of Directors of: CH Energy Group (Lead Independent Director; Chairman, Governance and Nominating Committee; Member, Audit; Previous Chairman, Audit Committee and Compensation Committee), National Regulatory Research Institute, Keystone Energy Board, and Regulatory Information Technology Consortium; Member, Wall Street Utility Group; Participant, Keystone Center Dialogues on RTOs and on Financial Trading and Energy Markets.

October 1993 – April 2002

Group Head and Managing Director; Senior Director -- Global Power Group, Fitch IBCA Duff & Phelps -- New York/Chicago

Manager of 18-employee (\$15 million revenue) group responsible for credit research and rating of fixed income securities of U.S. and foreign electric and natural gas companies and project finance; Member, Fitch Utility Securitization Team.

- Led an effort to restructure the global power group that in three years time resulted in 75% new personnel and over 100% increase in revenues, transforming a group operating at a substantial deficit into a team-oriented profit center through a combination of revenue growth and expense reduction.

- Achieved national recognition as a speaker and commentator evaluating the effects of regulatory developments on the financial condition of the utility sector and individual companies; Cited by Institutional Investor (9/97) as one of top utility analysts at rating agencies; Frequently quoted in national newspapers and trade publications including The New York Times, The Wall Street Journal, International Herald Tribune, Los Angeles Times, Atlanta Journal-Constitution, Forbes and Energy Daily; Featured speaker at conferences sponsored by Edison Electric Institute, Nuclear Energy Institute, American Gas Assn., Natural Gas Supply Assn., National Assn. of Regulatory Utility Commissioners (NARUC), Canadian Electricity Assn.; Frequent invitations to testify before U.S. Senate (on C-Span) and House of Representatives, and state legislatures and utility commissions.
- Participant, Keystone Center Dialogue on Regional Transmission Organizations; Member, International Advisory Council, Eisenhower Fellowships; Author, "A Rating Agency's Perspective on Regulatory Reform," book chapter published by Public Utilities Reports, Summer 1995; Advisory Committee, Public Utilities Fortnightly.

March 1994 – April 2002

Consultant -- NYNEX -- New York, Ameritech -- Chicago, Weatherwise USA -- Pittsburgh

Provided testimony before the Federal Communications Commission and state public utility commissions; Formulated and taught specialized ethics and negotiation skills training program for employees in positions of a sensitive nature due to responsibilities involving interface with government officials, marketing, sales or purchasing; Developed amendments to NYNEX Code of Business Conduct.

October 1987 - October 1993

Chairman; Commissioner -- Michigan Public Service Commission -- Lansing

Administrator of \$15-million agency responsible for regulating Michigan's public utilities, telecommunications services, and intrastate trucking, and establishing an effective state energy policy; Appointed by Democratic Governor James Blanchard; Promoted to Chairman by Republican Governor John Engler (1991) and reappointed (1993).

- Initiated case-handling guideline that eliminated agency backlog for first time in 23 years while reorganizing to downsize agency from 240 employees to 205 and eliminate top tier of management; MPSC received

national recognition for fashioning incentive plans in all regulated industries based on performance, service quality, and infrastructure improvement.

- Closely involved in formulation and passage of regulatory reform law (Michigan Telecommunications Act of 1991) that has served as a model for other states; Rejuvenated dormant twelve-year effort and successfully lobbied the Michigan Legislature to exempt the Commission from the Open Meetings Act, a controversial step that shifted power from the career staff to the three commissioners.
- Elected Chairman of the Board of the National Regulatory Research Institute (at Ohio State University); Adjunct Professor of Legislation, American University's Washington College of Law and Thomas M. Cooley Law School; Member of NARUC Executive, Gas, and International Relations Committees, Steering Committee of U.S. Environmental Protection Agency/State of Michigan Relative Risk Analysis Project, and Federal Energy Regulatory Commission Task Force on Natural Gas Deliverability; Eisenhower Exchange Fellow to Japan and NARUC Fellow to the Kennedy School of Government; Ethics Lecturer for NARUC.

August 1985 - October 1987

Acting Associate Deputy Under Secretary of Labor; Executive Assistant to the Deputy Under Secretary -- U.S. Department of Labor - Washington DC

Member of three-person management team directing the activities of 60-employee agency responsible for promoting use of labor-management cooperation programs. Supervised a legal team in a study of the effects of U.S. labor laws on labor-management cooperation that has received national recognition and been frequently cited in law reviews (U.S. Labor Law and the Future of Labor-Management Cooperation, w/S. Schlossberg, 1986).

January 1983 - August 1985

Senate Majority General Counsel; Chief Republican Counsel -- Michigan Senate -- Lansing

Legal Advisor to the Majority Republican Caucus and Secretary of the Senate; Created and directed 7-employee Office of Majority General Counsel; Counsel, Senate Rules and Ethics Committees; Appointed to the Michigan Criminal Justice Commission, Ann Arbor Human Rights Commission and Washtenaw County Consumer Mediation Committee.

March 1982 - January 1983

**Assistant Legal Counsel -- Michigan Governor William Milliken --
Lansing**

Legal and Labor Advisor (member of collective bargaining team); Director,
Extradition and Clemency; Appointed to Michigan Supreme Court
Sentencing Guidelines Committee, Prison Overcrowding Project,
Coordination of Law Enforcement Services Task Force.

October 1979 - March 1982

**Appellate Litigation Attorney -- National Labor Relations Board --
Washington DC**

Other Significant Speeches and Publications

- The "A" Rating (Edison Electric Institute Perspectives, May/June 2009)
- Perspective: Don't Fence Me Out (Public Utilities Fortnightly, October 2004)
- Climate Change and the Electric Power Sector: What Role for the Global Financial Community (during Fourth Session of UN Framework Convention on Climate Change Conference of Parties, Buenos Aires, Argentina, November 3, 1998)(unpublished)
- Regulation UnFettered: The Fray By the Bay, Revisited (National Regulatory Research Institute Quarterly Bulletin, December 1997)
- The Feds Can Lead...By Getting Out of the Way (Public Utilities Fortnightly, June 1, 1996)
- Ethical Considerations Within Utility Regulation, w/M. Cummins (National Regulatory Research Institute Quarterly Bulletin, December 1993)
- Legal Challenges to Employee Participation Programs (American Bar Association, Atlanta, Georgia, August 1991) (unpublished)
- Proprietary Information, Confidentiality, and Regulation's Continuing Information Needs: A State Commissioner's Perspective (Washington Legal Foundation, July 1990)